Memorandum

Date MAR - 2 1998

From Joseph J. Green
Assistant Inspector General
for Public Health Service Audits

Subject Report of Review of the Food and Drug Administration's Internal Controls Over Its Purchase Card Activities (A-15-97-80002)

To Robert J. Byrd
Deputy Commissioner for Management and Systems
Food and Drug Administration

The attached final report presents the results of the Office of Inspector General's review of internal controls over purchase card activities at the Food and Drug Administration (FDA). The report contains one recommendation to improve FDA's controls over its card purchases.

In responding to our draft report, FDA agreed with our recommendation. The FDA's comments are presented as Appendix A to this report.

We would appreciate your views and the status of any further action taken or contemplated on our recommendation within 60 days. If you have any questions, please call Frank Zuraf, Audit Director, at (301) 443-9766.

Attachment

Department of Health and Human Services

OFFICE OF INSPECTOR GENERAL

REVIEW OF THE FOOD AND DRUG ADMINISTRATION'S INTERNAL CONTROLS OVER ITS PURCHASE CARD ACTIVITIES

JUNE GIBBS BROWN
Inspector General

MARCH 1998
A-15-97-80002

OFFICE OF INSPECTOR GENERAL

The mission of the Office of Inspector General (OIG), as mandated by Public Law 95-452, as amended, is to protect the integrity of the Department of Health and Human Services (HHS) programs, as well as the health and welfare of beneficiaries served by those programs. This statutory mission is carried out through a nationwide network of audits, investigations, and inspections conducted by the following operating components:

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The OIG's Office of Audit Services (OAS) provides all auditing services for HHS, either by conducting audits with its own audit resources or by overseeing audit work done by others. Audits examine the performance of HHS programs and/or its grantees and contractors in carrying out their respective responsibilities and are intended to provide independent assessments of HHS programs and operations in order to reduce waste, abuse, and mismanagement and to promote economy and efficiency throughout the Department.

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Memorandum

Date MAR - 2 1998

From Joseph J. Green
Assistant Inspector General
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Subject Review of the Food and Drug Administration's Internal Controls Over Its Purchase Card Activities (CIN: A-15-97-80002)

To Robert J. Byrd
Deputy Commissioner for Management and Systems
Food and Drug Administration

This report provides you with the results of the Office of Inspector General's review of the Food and Drug Administration's (FDA) internal controls over its purchase card activities at its headquarters components.

The FDA began using the VISA purchase cards in 1989. The Purchase cards work much like personal credit cards, enabling designated FDA employees to purchase goods or services costing, for the most part, $2500 or less without much of the administration and paperwork required by the standard procurement system. In Fiscal Year (FY) 1996, FDA headquarters components used these cards to purchase goods and services totaling about $12 million.

The objective of our review was to determine whether FDA has designed and implemented adequate internal controls over its purchase card activities in its headquarters operations.

Generally, we found that FDA followed general guidelines provided by the General Services Administration (GSA) for the use of credit cards and designed and implemented adequate management controls over their use in its headquarters operations. We did find one problem regarding internal controls over the purchase card system. The FDA has not formally assessed the effectiveness of compensating controls over the use of purchase cards. Such controls are necessary because certain basic controls, such as separation of duties, are inherently missing in the purchase card system. We are recommending that FDA evaluate the effectiveness of compensating controls over the purchase card system.

Our review did find several minor problems with the use of purchase cards which we brought to the attention of FDA management and have reported in the Other Matters section of this report. We found that FDA had improperly paid State sales tax in 3 of 174 randomly selected transactions, and in one instance did not properly enter in its property management records 2 sensitive accountable property items. A sensitive item is one that is subject to unusual rates of loss, theft, or misuse. We also noted that the

FDA's Division of Accounting leased a software package for $24,900, to automate its purchase card activities without coordinating with FDA's Office of Information Resources Management (OIRM) which is responsible for such initiatives. The OIRM is currently implementing an agencywide Administrative System Automation project.

The FDA concurred with our recommendation, as well as in findings presented in the other matters section of the report. The FDA's comments are addressed in this report and are included in their entirety in Appendix A.

BACKGROUND

The GSA awarded a purchase card contract to Rocky Mountain BankCard System, Inc. (RMBCS) in 1989. Under this contract, GSA made RMBCS purchase cards available to all Government agencies. In this contract, GSA provided guidance to the Federal agencies for using the cards. However, it stated that it is the responsibility of each agency participating in the purchase card program to establish and implement its own internal procedures concerning the program.

In 1993, the National Performance Review (NPR) Report identified the purchase card as an acquisition reform that could save millions of dollars annually. The NPR Report recommended that all Federal agencies use purchase cards, and that the Federal Acquisition Regulations be amended to promote and facilitate purchase card use for making small purchases.

The card use was further facilitated in 1994 by the enactment of the Federal Acquisition Streamlining Act, Executive Order 12931, and an Office of Management and Budget memorandum to agency senior procurement executives. Also, in December 1994, an interim Federal Acquisition Regulation rule was issued making the card the preferred method for micro-purchases.[1] This rule also eliminated competition and other procurement requirements for micro-purchases.

The FDA implemented the purchase card system in 1989. Currently, all of FDA's components are using the cards. The FDA's headquarters operation consists of six centers, and the Office of the Commissioner (OC). Within this headquarters operation, FDA has 32 organizations that receive separate monthly invoices from RMBCS. The FDA currently has about 601 cardholders in its headquarters operation. The majority, 595 or 99 percent, of the cardholders were authorized transaction limits not to exceed $2,500, and only 6 were authorized transaction limits in excess of $2,500 and up to $25,000.

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[1] A micro-purchase is a purchase not to exceed $2,500.

In FY 1996, these headquarters cardholders used the cards to purchase goods and services amounting to about $12 million. The FDA officials told us that they do not anticipate that the headquarters operation will appreciably increase the card purchase volume in the coming years.

Under this purchase card program, cardholders can acquire goods and services, orally (telephonically) or in person, and charge the costs on a special Governmentwide VISA card, called International Merchant Purchase Authority Card (IMPAC), administered by RMBCS.

The FDA is currently performing all purchase card activities on a manual basis. The Division of Accounting (DOA) has leased a software package and is piloting a systems application to automate these activities.

Currently, the charges made are billed to each cardholder by RMBCS on the 5th day of each month for the immediately preceding month. The cardholders receive the statements of accounts from RMBCS a few days later, and reconcile their records of purchase logs to the billed charges. The cardholder attests to the accuracy of the charges as well as to the receipt of the purchased goods and services, or disputes charges if warranted. The cardholders make their monthly purchase logs, their reconciliations, and their monthly documentation of card purchases available to their card approving officials for their review and approval. Any purchase of sensitive accountable property needs to be approved by the Property Management Branch beforehand and manually entered into the personal property records.

The card approving officials are responsible for reviewing the cardholders' monthly logs for card purchases and the monthly statements of accounts, as well as the purchase documents. They are also responsible for approving payment for the purchases. Upon their approval, the statements of accounts, the purchase logs, the receiving or packing slips, and other documents are sent to the administrative offices to which they are assigned. Officials in the administrative sections accumulate the charges by appropriation, common accounting number, and object class; retain this documentation, and forward the summaries to the DOA for payment. The DOA is to make the payment within 30 days from the date of receipt.

The DOA and the Agency Program Coordinator conduct oversight reviews of the credit card operation. On a monthly basis, they select a random number of 20 percent of the cardholders and conduct reviews of the acquisition files of the selected cardholders. The reviews are focused on assessing the adequacy of the documentation and compliance with published procedures, as well as on identifying unauthorized purchases, and evidence of improper order splitting. In case of impropriety, FDA starts administrative actions, including criminal prosecution or disciplinary action, as appropriate.

OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of the review was to determine whether FDA has designed and implemented adequate internal controls over its purchase card activities.

We analyzed FDA's policy manual for the purchase card program to ascertain whether it provides adequate internal control procedures to protect FDA's interest and minimize the inherent risk of using purchase cards.

We reviewed audit reports on purchase card activities issued by various Federal departments and agencies and noted the problems cited in those reports to determine whether FDA's internal procedures for the card would guard against the occurrence of such problems.

We limited our review to FDA's headquarters. We obtained documentation for all FDA's card purchases made in November and December 1996, in FDA's headquarters. At that time, there were 601 cardholders who used the cards to purchase goods and services amounting to $1.1 million during those 2 months.

We randomly selected 30 of these cardholders and reviewed the official records for all of their card purchases made during November and December 1996, to ascertain whether they were in compliance with the FDA's internal procedures. During the 2-month period, these 30 randomly selected cardholders made 174 card purchases amounting to $57,079.

We interviewed the cardholders who made the sampled transactions and the card approving officials with oversight responsibilities over the cardholders. We interviewed FDA's Agency Program Coordinator, as well as officials in FDA's property management, accounting operation, and OIRM.

In addition, we reviewed General Accounting Office"s (GAO) Title 2, Policies and Procedures Manual for Guidance of Federal Agencies (Manual). This Manual includes general and specific internal control standards. We evaluated FDA's compliance with the separation of duties standard because the separation of duties was reported as a problem in most of the audit reports we obtained from other Federal agencies concerning the card use. We also obtained and reviewed information from FDA's OIRM.

We performed our review of 5 centers and 10 offices at FDA's headquarters, located in the Washington Metropolitan area. We conducted our review in accordance with generally accepted government auditing standards between March and September 1997.

FINDINGS IN DETAIL

FDA'S ASSESSMENT OF COMPENSATING CONTROLS OVER PURCHASE CARDS

The FDA has not formally assessed the effectiveness of compensating controls over the use of purchase cards. Compensating controls are required when certain basic internal controls, such as the separation of duties, are missing. Under the purchase card system in FDA, this basic control is inherently missing because the same individual cardholder is allowed to order, receive, and then sign for the receipt of goods and services purchased with the card. Compensating controls could include reviews to ensure that such purchases were properly documented and that the items purchased are also received. When basic controls are missing, it is important to ensure that such compensating controls are working as intended.

The GAO has provided guidance to Federal agencies on internal controls in its Manual, referred to as Title 2. Appendix II of Title 2, Specific Standard 4, Separation of Duties, states that to reduce the risk of error, waste, or wrongful acts, or to reduce the risk of them going undetected, key duties are to be separated between different officials. Key duties include authorizing, approving and recording transactions, issuing and receiving assets, making payments, and reviewing or auditing transactions.

Our review of 174 card purchases made by 30 randomly selected cardholders during November and December 1996, showed that 17 cardholders ordered and received, as well as attested to receiving the ordered goods. The Associate Director for Acquisition told us that FDA has compensating controls to allow for this lack of separation of duties in the card purchasing activity. He said that card approving officials are responsible for reviewing the cardholders' monthly files to ascertain that all the purchases are for official purposes, and are properly documented. He also said that these approving officials usually approve purchases beforehand. However, he said that such compensating controls have not been formally assessed for adequacy and effectiveness. We did not evaluate the adequacy of these compensating controls. However, we agree that this combination could reduce FDA's vulnerability to error, waste, or wrongful acts.

RECOMMENDATION:

We recommend that FDA fully evaluate the adequacy of controls over the purchase card program which FDA believes compensate for the lack of separation of duties.

Agency Comments

The FDA concurred with the recommendation, and stated that it has established a team to evaluate the adequacy and effectiveness of compensating controls over its purchase card activities.

OTHER MATTERS

(This section of our report discusses issues which were identified during our review but did not involve serious departures from policy or procedures or result in major system deficiencies that require recommendations to management for corrective action. These issues are reported here so that procedural errors might be corrected, where appropriate, and to serve as a reminder that these issues, if not monitored on a continuing basis, might evolve into more serious problems.)

State Sales Taxes

The FDA instructs cardholders not to pay State sales taxes. Our review of 174 card purchases made in November and December 1996, by the 30 randomly selected cardholders showed that 3 cardholders erroneously paid State sales taxes on 3 purchases. We brought these errors to the attention of the involved cardholders and card approving officials who are responsible for reviewing the monthly card purchases and approving them for payment. These officials acknowledged that the sales taxes were paid in error. After we brought the erroneous payments to their attention, one of the officials secured a refund for the State sales taxes, and the others stated that they will try to do the same.

Agency Comments

The FDA stated that it will continue to emphasize to cardholders and approving officials during training sessions that they should not pay State sales taxes.

Accounting for Sensitive Property

Our review of all the purchases made in November and December 1996, by the 30 randomly selected cardholders showed that one of those cardholders purchased two sensitive and accountable property items which were not properly accounted for and included in the property management records, as required by FDA's Bankcard Manual. FDA's Handbook For Property Custodial Officer states that accountable property consists of all Government property items costing $5,000 or more, and items costing less than $5,000 that require special control, or are determined to be subject to unusual rates of loss, theft, or misuse (sensitive property). The handbook states that such

property items are to be reported to the Personal Property Management Section and are to be included in the property management system.

The property custodian involved in this instance attributed the two items not included in the property management system to an oversight. She also said that based on our inquiry, she has now included these items in the property management system. She said that she also found that other items that should have been recorded in the system were not, and that she will record them in the property system accordingly.

Agency Comments

The FDA stated that it will send a memorandum to all cardholders and approving officials reminding them of their responsibilities under the purchase card program.

Automating Purchase Card Activities

Our review also showed that FDA's DOA has leased a software package to pilot a systems application to automate FDA's purchase card activities. The lease agreement cost $24,900, and entitled FDA to pilot the systems application for 1 year only in the OC's headquarters operation. The DOA is planning to implement this systems application throughout FDA's headquarters operation at a probable cost in excess of $25,000.

The DOA did not coordinate this effort with OIRM, even though OIRM has the responsibility to coordinate systems development in FDA. The FDA officials told us that it is FDA's policy that OIRM does not review systems application purchases costing less than $25,000. We also found that OIRM is in the process of implementing an agencywide Administrative System Automation project.

In view of the fact that: (1) this systems application is administrative in nature; (2) the DOA intends to implement this systems application throughout the centers and offices in the headquarters operation and possibly in the field offices; and (3) that the annual cost of the lease of the systems application software package will be greater than the $25,000 threshold that would require OIRM review, we believe that this systems application should be coordinated with OIRM before it is implemented throughout the FDA's headquarters.

Agency Comments

The FDA stated that should the systems application software package to automate its purchase card activities be expanded beyond the pilot project, the package will be processed through the OIRM for review.

APPENDIX

DEPARTMENT OF HEALTH & HUMAN SERVICES

Public Health Service
Food and Drug Administration

Memorandum

Date: FEB 23 1998

From: Deputy Commissioner for Management and Systems, FDA

Subject: FDA Comments on OIG Draft Report, Review of the Food and Drug Administration's Internal Controls Over its Purchase Card Activities" - A-15-97-80002

To: Joseph J. Green
Assistant Inspector General
for Public Health Service Audits

We have reviewed the Office of Inspector General's draft report, "Review of the Food and Drug Administration's Internal Controls Over its Purchase Card Activities," and submit the attached FDA comments. FDA concurs with the report's recommendation and "other matters" highlighted in the report, and will take action to implement the recommendation.

Robert J Byrd

Robert J. Byrd

Attachment

AGENCY COMMENTS ON THE OFFICE OF INSPECTOR GENERAL DRAFT REPORT, "REVIEW OF THE FOOD AND DRUG ADMINISTRATION'S INTERNAL CONTROLS OVER ITS PURCHASE CARD ACTIVITIES" (A-15-97-80002)

OIG Recommendation

That FDA fully evaluate the adequacy of controls over the purchase card program which FDA believes compensate for the lack of separation of duties.

FDA Comment

We concur with the intent of this recommendation.

In response, the Office of Management and Systems (OMS) has established a team to review the internal controls each Center/Office has in place. Specifically, the team will evaluate the adequacy and effectiveness of compensating controls over its purchase card activities. The team is comprised of selected staff members from the Office of Financial Management (OFM), the Office of Human Resources and Management Services (OHRMS), and the Office of Facilities, Acquisitions and Central Services (OFACS). The team will:

- Review the internal control procedures the Center/Office has in place;
- Interview a sample of approving officials and inspect the documents supporting their monthly review; and
- Interview a sample of card holders to ascertain the frequency and methods of communication with their cognizant approving official.

Other Matters Identified

State Sales Tax

During training sessions for card holders and approving officials, FDA will continue to emphasize the nonpayment of sales tax.

Accounting for Sensitive Property

A memorandum will be sent to all card holders and approving officials reminding them of their responsibilities under the International Merchant Purchase Authority Card (IMPAC) Program.

Automating Purchase Card Activities

Should the systems application software package to automate FDA's purchase card activities be expanded beyond the pilot, the package will be processed through the Office of Information Resources Management (OIRM) for review.